

Interagency Task Force on Employee Misclassification

Report to
Governor Jennifer M. Granholm

July 1, 2008

Keith W. Cooley
Task Force Chair and
Director, Michigan Department of
Labor & Economic Growth



Executive Summary

Employee misclassification is a growing problem throughout Michigan and the nation. The federal Government Accountability Office recently estimated that employee misclassification resulted in the underpayment of an estimated \$2.72 billion in Social Security taxes, unemployment insurance (UI) taxes and income taxes in 2006. While such estimates are not available for Michigan, the state's UI Trust Fund has suffered significant losses due to unpaid UI taxes arising from employee misclassification.

In response to the problem, Governor Jennifer Granholm issued Executive Order 2008-1, establishing the Interagency Task on Employee Misclassification. The task force is comprised of three agencies from within the Department of Labor & Economic Growth – Unemployment Insurance Agency, Wage & Hour Division, and Workers' Compensation Agency – as well as the Departments of Treasury and Management & Budget.

The task force has been directed to study the problem of employee misclassification, develop ways of improving communication and public awareness of the problem, coordinate and strengthen enforcement mechanisms in the state and other jurisdictions and make recommendations for legislative action where needed.

Misclassification most commonly occurs when an employer hires a worker and improperly classifies the worker as an "independent contractor," rather than as an "employee." The practice is harmful to employers, workers and taxpayers. Employee misclassification creates an unfair competitive advantage for employers, prevents misclassified employees from receiving certain benefits and causes government to lose out on important tax revenues.

As the Department of Treasury noted, "The understated taxes of these employers and employees means less revenue to the state and less funds for K-12 education, local units of government, health and social programs, colleges, and police and fire protection."

Since its inception, the Task Force has held three public meetings and one public hearing. Other public hearings around the state are scheduled for the summer of 2008. The Task Force has also established three subcommittees – Legal, Education & Communications, and Research.

A website has been created and linked from the DLEG Home Page (www.michigan.gov/dleg). The website has information about the issue and Task Force updates. A toll-free telephone number – 1-800-822-1122 – has also been set up to accept tips on suspected employee misclassification.

The Unemployment Insurance Agency (UIA) has joined the national Questionable Employment Tax Practices program and is sharing information with the Internal Revenue Service that will improve compliance with state and federal regulations governing employment and unemployment tax activities and help reduce worker misclassification. The agency is also working with 1099-Misc. information from the IRS in identifying potential employee misclassification. In using this information, UIA has identified \$23.3 million misclassified wages from 2003 to 2007.

The Task Force has also been in contact with other states is gathering and sharing information about best practices for combating employee misclassification.

**Report to Governor Jennifer M. Granholm
Interagency Task Force on Employment Misclassification
July 1, 2008**

Introduction

In February 2008, Michigan Governor Jennifer M. Granholm issued Executive Order 2008-1, establishing an Interagency Task Force on Employee Misclassification.

The task force was charged with examining the problem of employee misclassification, developing ways of improving communication and public awareness of the problem, coordinating and strengthening enforcement mechanisms in the state and with other jurisdictions, and recommending legislative action, where needed. Since the issue cuts across state government, the Governor sought a coordinated and effective approach to the problem.

Task Force members

The Executive Order names the Department of Labor & Economic Growth (DLEG) director to chair the task force and appoints as members individual representatives from DLEG's Unemployment Insurance Agency, Wage & Hour Division, and Workers' Compensation Agency, and from the Business Services Administration within the Department of Management & Budget and from the Discovery and Tax Enforcement Division within the Department of Treasury.

The task force members are:

- o Keith W. Cooley, Director, Michigan Department of Labor & Economic Growth, and Task Force Chair
- o Jack Nolish, Director, Workers' Compensation Agency, DLEG
- o Director, Unemployment Insurance Agency, DLEG
- o Jack Finn, Administrator, Wage & Hour Division, DLEG
- o Douglas Schafer, Director, Tax Compliance Bureau, Michigan Department of Treasury
- o B. Craig Orr, Director, Business Service, Michigan Department of Management & Budget

Agency descriptions

Management & Budget

DMB Business Services provides a wide range of services for the state of Michigan's 19 agencies and departments. These services include purchasing, facilities, vehicle fleet operations, print and graphics, mail & delivery and retirement services.

Treasury

The Tax Compliance Bureau of the Michigan Department of Treasury enforces compliance with state of Michigan tax statutes through its Large and Mid-Size Business Division, Small Business and Special Teams Division, and the Discovery and Tax Enforcement Division.

Labor & Economic Growth

The Michigan Department of Labor & Economic Growth (DLEG) is composed of labor and economic development agencies and commissions that promote job creation and economic growth in Michigan by centralizing and streamlining the state's job development, workforce development, and economic development functions under one department. Within the department are:

- Unemployment Insurance Agency
The Unemployment Insurance Agency (UIA) helps jobless workers and their families by providing a temporary income while the workers are unemployed and seeking new employment. Unemployment insurance helps employers by keeping a skilled work force on hand until jobs become available. It also aids the economy as unemployment benefits are "high velocity" dollars that are used quickly to purchase local goods and services.
- Wage & Hour Division
The Wage & Hour Division administers the state laws that protect the wages and fringe benefits of Michigan's workers and provide for the safe and legal employment of minors
- Workers' Compensation Agency
The Workers' Compensation Agency administers the Workers' Disability Compensation Act, which provides wage replacement, medical, and vocational rehabilitation benefits to men and women who suffer work-related injuries and disabilities. The Agency also assures compliance with the mandatory insurance provisions of the act to protect injured workers and to protect Michigan employers from unfair competition by those who are not in compliance.

What is employee misclassification?

Misclassification most commonly occurs when an employer hires a worker and improperly classifies the worker as an "independent contractor," rather than as an "employee."

The difference between an independent contractor and an employee is determined in part by the concept of "right to control." With an employee, the employer determines what needs to be done (results) and controls how it is to be done (means). The person is normally directed by the employer.

Independent contractors, on the other hand, are *not* employees but are in business for themselves. They are hired to accomplish a task or tasks as determined by the employer, but independent contractors retain the right to control how they will get the work done.

They, usually, make themselves available to the employer community at large and do not limit themselves to performing services for a single company. Independent contractors usually supply their own tools.

Consequences of employee misclassification

The misclassification of employees impacts employers, workers and government. Misclassified employees may not qualify for certain benefits; tax-abiding employers are placed at a competitive disadvantage, while government loses important tax revenues.

Nationally, the Government Accountability Office reports that employee misclassification resulted in the underpayment of an estimated **\$2.72 billion** in Social Security taxes, unemployment insurance (UI) taxes and income taxes in 2006. In Michigan, the state's UI Trust Fund has suffered significant losses due to unpaid UI taxes, while the state has lost important tax revenues because of employee misclassification. Employee misclassification has been identified, along with SUTA Dumping, as two top enforcement priorities by the U. S. Department of Labor.

SUTA (state unemployment tax act) Dumping is a tax evasion practice involving the manipulation of an employer's unemployment insurance (UI) tax rate to achieve a lower rate, and thereby pay less UI taxes. Typically, SUTA Dumping occurs when a business transfers payroll out of an existing company or organization to a new or different organization solely or primarily to reduce UI taxes.

The misclassification of wages is an important issue to labor. For **workers** whose wages are misclassified, they may:

- Be ineligible for payments such as UI and workers' disability compensation
- Lose other labor law protections such as minimum and prevailing wage, overtime, health and safety, and family and medical leave
- Become liable for their full Social Security taxes and have to report their own income taxes. When the employee is paid in cash, neither the employee nor the employer may pay FICA/Social Security taxes. Consequently, the employee may receive less in Social Security benefits at retirement as the unreported wages are not credited toward the employee's potential Social Security entitlement.
- Lose access to employer-based benefits, such as health insurance

Companies that follow the rules are placed at a significant competitive disadvantage compared to those that call their workers "independent contractors." **Employers** that misclassify their employees' wages:

- Gain an unfair competitive business advantage allowing them to underbid employers who do not misclassify their employees by:
 - Avoiding the payment of income taxes, FICA taxes, unemployment taxes and workers' compensation premiums on workers that they do not classify as employees
- Potentially avoid some state and federal laws, ranging from anti-discrimination legislation to wage and hour protections, which typically govern the employer-employee relationship but may not apply to independent contractors.

Taxpayers suffer a loss when workers are misclassified, due to:

- Underreporting of UI taxable wages, resulting in the collection of less UI taxes to pay benefits, which means other employers pay higher UI taxes in order to cover benefit costs
- Uncollected income taxes and FICA taxes as some workers who receive 1099-MISCs fail to report their earnings and pay the taxes owed, and the employers are not paying their true share of FICA taxes on these workers.

Michigan started taking action on the misclassification problem in 2004, when it established the Misclassification of Wages Unit within the UIA Tax Office. The Agency has also partnered with its sister agencies around the country taking an aggressive stance with employers that are inappropriately using 1099s. UIA is sharing information and best practices and is investigating complaints jointly with the Wage & Hour Division and the Workers' Compensation Agency.

Nationally, Michigan was the first state to sign a Questionable Employment Tax Practices memorandum of understanding (MOU) with the IRS. The MOU was signed in November 2007; it outlines additional ways UIA and IRS can work together to ensure that all employers are paying their fair share of employment and unemployment taxes.

The Charge to the Task Force

In creating the Interagency Task Force on Employee Misclassification, the Governor set forth a number of expectations for the Task Force. They include:

1. Examine and evaluate existing employee misclassification enforcement mechanisms in Michigan and other jurisdictions, and make recommendations for more effective enforcement mechanisms. In particular, the Task Force should examine and evaluate the existing employee misclassification enforcement mechanisms arising under the Minimum Wage Law of 1964, 1964 PA 154, MCL 408.381 to 408.398; 1978 PA 390, MCL 408.471 to 408.490; the Michigan Employment Security Act, 1936 (Ex Sess) PA 1, MCL 421.1 to 421.75; the Worker's Disability Compensation Act of 1969, 1969 PA 317, MCL 418.101 to 418.941; 1965 PA 166, MCL 408.551 to 408.558; and the Income Tax Act of 1967, 1967 PA 281, MCL 206.1 to 206.532.
2. Create a system for sharing information relating to suspected employee misclassification violations among Task Force member agencies, to the extent possible under existing Michigan law.
3. Establish a protocol through which individual Task Force member agencies investigating employee misclassification matters under their own statutory or administrative authority will refer a matter to other Task Force member agencies for assessment of potential liability under other relevant authority.
4. Explore information sharing possibilities with investigators in other jurisdictions.

5. Identify barriers to information sharing under current state law and recommend to the Governor proposed executive or legislative actions needed to overcome the barriers.
6. Facilitate the pooling, focusing, and targeting of investigative resources, to the extent possible under current Michigan law.
7. Develop strategies for systematically investigating employee misclassification within those industries in which misclassification is most common.
8. Identify significant cases of employee misclassification that should be jointly investigated and, to the extent possible under existing Michigan law, form joint enforcement teams to utilize the collective investigative and enforcement capabilities of Task Force member agencies.
9. Work cooperatively with local, state, and federal law enforcement agencies, including sharing information with the Internal Revenue Service and establishing a systematic procedure for referring cases to the Attorney General or local or federal prosecutors.
10. Work cooperatively with state, federal, and local social services agencies to provide assistance to workers that have been exploited by employee misclassification.
11. Work cooperatively with business, labor, and community groups interested in reducing employee misclassification, including but not limited to both of the following:
 - a. Seeking ways to prevent employee misclassification, such as through the dissemination of educational materials regarding the legal differences between independent contractors and employees.
 - b. Enhancing mechanisms for identifying and reporting instances of employee misclassification.
12. Consult with representatives of business, organized labor, and other entities, including the Michigan Economic Development Corporation, about the employee misclassification enforcement activities of the Task Force and its member agencies, and ways of improving operations.
13. Increase public awareness of the illegal nature of and harms inflicted by employee misclassification.
14. Establish procedures for soliciting referrals or information from the public, including through a telephone hotline.

TASK FORCE ACCOMPLISHMENTS

Public meetings

Since its creation, the Task Force has held three public meetings – March 27, 2008, in Detroit; May 20, 2008, in Lansing; and June 17, 2008, in Lansing.

Subcommittees established

The Task Force has established three working subcommittees – Legal, Research and Education/Communications. Each subcommittee is chaired by a Task Force member and is composed of volunteers from the public as well as staff from the participating departments and agencies.

Legal subcommittee:

The initial task for the Legal Committee was to examine how the various Michigan statutes define the term “employee.” In its research, the committee examined the Workers’ Disability Compensation Act, the Michigan Employment Security Act, the Minimum Wage Law, the Michigan Business Tax, the Michigan Income Tax, the Michigan Occupational Safety and Health Act, and the Prevailing Wage Law. It found that there are variations in how the term “employee” is defined by each of the laws. The committee produced the following matrix reporting on how various state statutes define “employee:”

Public Act	Definition of employee (does not cover certain professions or trades that have specific statutory authority)
Workers Disability Compensation Act MCL 418.161(1)(n)	Every person performing service in the course of a trade, business, profession or occupation of an employer at the time of injury, if the person in relation to this service does not maintain a separate business, does not hold himself or herself out to and render service to the public, and is not an employer subject to this act. Case law requires all three conditions to be met and removed the broader common law economic reality test after the definition was amended
Michigan Employment Security Act MCL 421.42(1)	“Employment” means service, including service in interstate commerce, performed for remuneration, or under any contract of hire, written or oral, expressed or implied.” Case law applies the economic reality test : <ul style="list-style-type: none"> • Control of worker’s duties • Payment of wages • Right to hire and fire • Right to discipline • The performance of duties as an integral part of the employer’s business towards the accomplishment of a common goal

Minimum Wage Law MCL 408.382.(b)	<p>“Employee” means an individual not less than 16 years of age employed by an employer on the premises of the employer or at a fixed site designated by the employer, and includes a minor employed under section 15(1) of the youth employment standards act.”</p> <p>Case law applies the economic reality test.</p>
MI Business Tax MCL 208.1109(1)	<p>“Employee” means an employee as defined in section 3401(c) of the internal revenue code.</p>
MI Income Tax MCL 206.8(2)	<p>IRC Reg 31.3401(c)-1(b) . . . exists when the person for whom the services are performed has the right to control and direct . . . not only as to the result. . . but also as to the details and means by which that result is accomplished.</p> <p>Factors to consider: right to discharge, supplies tools, supplies place to work</p>
MI Occupational Safety and Health Act MCL 408.1005(1)	<p>“Employee” means a person permitted to work by an employer.</p> <p>Case law interpretation: any individual receiving financial return from a business for work performed is an employee.</p>
Prevailing Wage Law MCL 408.551(a)	<p>“Construction mechanic” means a skilled or unskilled mechanic, laborer, worker, helper, assistant, or apprentice working on a state project but shall not include executive, administrative, professional, office or custodial employees.</p> <p>No case law, but department interpretation of employee relationship uses the economic reality test.</p>

Education & Communications subcommittee

This Committee is comprised of members from Michigan labor unions, a law student and representatives from state government. As its first task the committee set out to develop a PowerPoint presentation about the issue of Employee Misclassification, the Governor’s Executive Order, the Governor’s charge to the Task Force and how employee misclassification is harmful to workers, employers, government and taxpayers. The PowerPoint presentation will be used as an introduction to the public hearings that will be held around the state in the summer of 2008. The committee also wants to educate and inform the public about the issue of employee misclassification. The committee will also explore working with other groups that may be interested in the issue and will schedule a program about employee misclassification on an upcoming “Consumer’s Corner” cable television program hosted by Director Cooley.

Research subcommittee

The Research subcommittee is composed of members from Michigan labor unions and state government. It will be examining various state and national studies that have been prepared on the issue of misclassification as well as the underground economy. The subcommittee will also study what other states and organizations, such as the Internal Revenue Service, are doing to deter employee misclassification and look at their best practices. In addition, the group will review methods for enforcement and ways to prioritize leads, tips and referrals.

Website established

One of the first steps the Task Force took was the creation of a website that is linked from the Department Labor & Economic Growth's Home Page (www.michigan.gov/dleg). The site has basic information in a fact sheet about employee misclassification, as well as a link to the Governor's Executive Order 2008-1 and a toll-free telephone number (**1-800-822-1122**) that the public can call to report potential cases of employee misclassification. With little publicity, the hotline had received about 10 phone calls by the end of June referring potential employee misclassification cases to the Task Force.

In fact, a current employee misclassification investigation resulted from a call to the toll-free tip line. The investigation is one of three the Unemployment Insurance Agency is conducting that involve trucking companies that have classified their drivers as independent contractors and not as employees. One of the trucking/delivery firms came to the Agency's attention as a result of a call to the tip line. Some of the company's drivers have also spoken at public meetings of the Task Force.

All three investigations are currently underway to determine if the companies owe unemployment taxes and if the workers are independent contractors or employees.

Questionable Employment Tax Practices (QETP)

The Unemployment Insurance Agency is working with other states and the Internal Revenue Service (IRS) on the national QETP project. Through a Memorandum of Understanding 29 states, including Michigan, entered into information-sharing agreements with the IRS. Michigan, in fact, was the first state to sign the MOU.

The QETP agreement provides, for the first time, a centralized and uniform mechanism for exchanging employment tax data between IRS and state workforce agencies, such as Michigan's UIA. The agreement will help improve compliance with state and federal regulations governing employment and unemployment tax activities and reduce fraudulent filings and the misclassification of workers.

The UIA-IRS data exchange is also helping to strengthen employer compliance with Michigan's UI tax law and to help ensure that the state's unemployment tax system is fair for all employers, while helping to increase the collection of state and federal unemployment/employment tax debts.

The IRS - state agreement also encourages coordinated outreach and education activities, allowing all of the participating parties to present a consistent message and to encourage businesses to voluntarily meet their employment/unemployment tax responsibilities.

1099-Misc. data from IRS

UIA established an independent contractor unit in 2004 to investigate potential 1099 abuses. The Agency began receiving 1099-Misc. extracts from the IRS. These extracts

contain the names of those companies that issue the 1099-Misc to independent contractors as well as the names of the workers who receive these 1099s.

These extracts contain such information as the name, address, and Social Security number of the worker and how much was reported on their 1099-Misc. The extracts report the names and addresses of the employers issuing the 1099-Misc., along with their Federal Employer ID Number.

The UIA uses these extracts in selecting employers that will be audited to ensure that the workers are properly classified and that the proper amount of unemployment taxes are reported and paid. The extracts also help ensure that listed employers are registered with the Agency.

The table below reports findings from 1099-Misc. audits conducted by UIA from 2003 to 2007. The table shows that more than \$23.3 million in wages have been misclassified. The 2007 data is incomplete as the Agency is still performing audits for that tax year.

Audit Year	Number of 1099-M Audits	Misclassified Independent Contractors	Misclassified Casual Laborers	Gross Misclassified Wages
2003	8	35	28	\$402,396.88
2004	52	450	293	\$5,113,992.63
2005	234	687	570	\$9,282,224.02
2006	478	455	749	\$7,949,699.88
2007	20	25	44	\$576,186.10
	665	1652	1684	\$23,324,499.51

Coordination within DLEG

Prior to the Governor’s Executive Order, DLEG had started to coordinate its enforcement efforts by having UIA partner with its sister agencies -- Wage & Hour Division and the Workers’ Compensation Agency – in an aggressive stance with employers who are inappropriately using 1099s. The agencies continue to share information, best practices and investigate complaints. In addition, as a result of Task Force meetings, the Michigan Occupational Safety & Health Administration (MIOSHA) is also sharing information, when its staff encounters potential employee misclassification while visiting job sites.

Contact with other states

The Unemployment Insurance Agency has been contacted by neighboring states about Michigan’s efforts to combat employee misclassification. At the same time, UIA has been contacting other states about their efforts. The Agency is also an active participant in the national Questionable Employment Tax Practices (QETP) project with the IRS and serves on the oversight team with the IRS and several states, including

New York and California. The QETP project is providing UIA and Michigan with valuable contacts and information for its employee misclassification efforts.

Governor Deval Patrick of Massachusetts recently established a joint task force to bring the underground economy to the surface and to stop businesses from undermining fair competition. Gov. Patrick said he wants Massachusetts to join Michigan, California and New York as “leaders in targeting the underground economy.”

RAMIFICATIONS OF MISCLASSIFICATION AND TOOLS FOR ENFORCEMENT

The departments and agencies represented on the Task Force are the most significantly affected by employee misclassification. The impacts that employee misclassification has on the publics served by each of the agencies/departments are:

Unemployment Insurance Agency

Misclassification of wages impacts the unemployment insurance program in several ways. Workers who are unemployed and have 1099s are not covered by Michigan’s unemployment insurance law and are not eligible for UI benefits.

If an employer employs a worker as an independent contractor and issues the person a 1099, the worker is not considered an employee. As a result, the employer saves on state unemployment taxes. Other employers are affected as they pay a larger amount of UI taxes because other businesses are not paying their fair share.

If a person files an unemployment claim and was a 1099 worker with no reported wages, UIA will assign a field auditor to visit that business to make a liability determination to determine if the employer owes any unemployment taxes and if the worker is entitled to benefits. The agency also does random audits and targets audits when it receives information from the IRS about employers that have issued 1099s or tips from further sources, including other employers.

When an employer is found to have not paid their taxes due to fraud, the Employment Security Act provides a penalty against the employer of up to four times the amount they should have paid in unemployment taxes.

Workers’ Compensation Agency

The misclassification of workers as independent contractors or subcontractors impacts on employers’ compliance with Michigan’s Workers’ Disability Compensation Act. Michigan is a mandatory coverage state. Employers that have three or more employees at one time, and that also satisfy other criteria, must secure appropriate insurance coverage for workers’ compensation or be approved for self-insured status by the Agency. Once the required proof of coverage is filed, the carrier is liable for full statutory benefits for all the employer’s injured workers. The job classifications used to determine premium costs do not determine the issues in a workers’ compensation claim and do not impact on the amount and nature of the benefits that may be awarded.

Since the Agency does not review the contract between an employer and its carrier, we have no information on the premium impact brought about by improper job classification of workers for rate purposes.

Employers that avoid appropriate coverage or that choose self-insured status do so at their peril on several levels: They can be fined, closed down, held liable in civil court without the protection of the exclusive remedy limitations, and the officers/directors can be subjected to individual liability for the sanctions notwithstanding a corporate veil. The procedures to actually close a business are handled by the Attorney General through court action.

It can be difficult to identify non-compliant employers. To overcome this problem, WCA partners with MIOSHA and UIA, whose field auditors check for WC coverage when they do audits and job site inspections. Leads provided from these sister agencies are then subjected to inquiry by WCA compliance division. Employers are contacted regarding insurance coverage and appropriate sanctions are levied. From 1999 through 2007, about \$2.6 million has been collected in non-compliance fines.

If an injured worker files a workers' compensation claim, the Magistrate has the authority to determine that a worker was an employee at the time of injury, and therefore subject to the act and eligible to receive benefits even if the employer may have described the worker as independent contractor. If the injured worker's employer is a subcontractor on a job site and is uninsured, the worker's claim for benefits is against the general contractor on the job. There is concern that injured workers who could be eligible for benefits do not file claims thinking, erroneously, that they are subcontractors and not entitled to file a claim.

Wage & Hour Division

The Wage & Hour Division administers several of the state's labor laws. Worker misclassification has the greatest impact on the Prevailing Wage law. The employer may subcontract out and the subcontractor may say everyone is an independent contractor. The law does not provide penalties for such misclassifications.

The Payment of Wages and Fringe Benefit Act, however, does provide for penalties and interest for violations. The Minimum Wage and Overtime Law also carries penalties that the Division can enforce.

Department of Management & Budget

For DMB Business Services Administration, misclassification impacts the department through contracts for products and/or services needed by divisions with prime vendors and their subcontractors, which may have misclassified their employees. State contract language requires vendors to carry certain types of insurances, such as workers' disability compensation. Contractors are required to provide the necessary documentation showing coverage for both prime- and subcontractors before beginning work on a State project. In addition, contractors are required to have **the State named as an additional insured** on all contracts for commodities and/or services for each of

the divisions, except for professional liability insurance on professional services contracts.

Employee misclassification also impacts Business Services in the area of prevailing wage. When employees are misclassified, they may not be represented appropriately in the labor market and, thus, may be exempted from receiving the appropriate prevailing wages in cases where their skills and work functions would normally require it. Construction and furniture projects are the two areas in which prevailing wage affects DMB.

DMB Facilities, Building Operations, and Design & Construction are impacted similarly; but even more intensely in the area of prevailing wage, and misclassification issues surrounding relationships between prime- and subcontractors. Since many State construction projects use a general contractor to manage all parts of the job, keeping the classification area clear of problems becomes more complex for this area of DMB.

Enforcing these provisions is preventative, as work cannot begin, and a contractor will not be paid for work started before the contractor submits documentation of the necessary insurance coverage. This is done to prevent the State from being in situations where it will be held financially responsible for costs resulting from injury to contractor employees that are not covered by workers' compensation insurance.

State contracts also include provisions for indemnification, termination and, often, liquidated damages. Depending on the potential damages to the State resulting from misclassification, any of these other clauses can be used for enforcement and to prevent expenditures to vendors who misclassify employees.

Department of Treasury

If employers are paying employees "under the table," not only are they not paying several different taxes, they probably are not paying the right amount of individual taxes. If a worker is misclassified, that person may be reporting expenses they are not entitled to claim.

Employers who misclassify employees as independent contractors and issue 1099s to the individuals underpay withholding taxes, and single business tax. Single Business tax is underpaid, because wage compensation add-backs are understated, and various tax credits, primarily the small business credit or alternative tax credits, are overstated.

If employers pay employees under the table or off the books, the unreported wages probably result from unreported business receipts that are also off the books. These employers underpay withholding taxes, single business tax, sales tax and if the employer is a sole proprietor, their own individual income tax.

Individuals who are paid under the table will either not file a Michigan income tax return or will under-report their earnings. By not including their cash wages, individuals, who are misclassified as independent contractors by their employers and receive a 1099, will

under pay their Michigan income tax as they will claim expenses that true employees are not entitled to claim. They will file a Schedule C Profit or Loss from Business as a Sole Proprietorship claiming car or truck expenses, depreciation, insurance, lease expenses, supplies, travel, or meals – none of which they are entitled to claim as expenses, but all reduce earnings in calculating federal adjusted gross income, which is the starting point of the Michigan individual income tax return.

The understated taxes of these employers and employees means less revenue to the state and less funds for K-12 education, local units of government, health and social programs, colleges, and police and fire protection.

FORTHCOMING ACTIVITIES

Public Hearings

The Task Force has scheduled public hearings during the summer of 2008 at various sites around the state. Hearings are scheduled for June 30 in Farmington, July 10 in Benton Harbor and September 16 in Lansing. Hearings will also be held in Flint/Saginaw, Marquette and Traverse City.

Lt. Governor John Cherry is expected to attend several, if not all, of the hearings to hear testimony, along with the Task Force, from members of the public as well as from representatives of business and labor.

Joint audits/Investigations

The Task Force will examine the possibility of conducting joint audits of employers potentially involved in employee misclassification. The audits would be conducted by auditors from the Task Force member agencies and departments. The Task Force will also study the feasibility of exchanging audit information between the member agencies and departments.

UIA, for example, exchanges information with the Internal Review Service as part of the QETP project and has been receiving 1099 extract information from the IRS, which is used to investigate employers who issue 1099s to those it employs.

UIA is also developing a letter to employers who have been identified as issuing more 1099s than typical for their industry. The letter would ask these employers to provide information to the agency in lieu of having a field auditor visit the employer.

**Notes from Public Meetings of
The Interagency Task Force on
Employee Misclassification**

June 17, 2008
May 20, 2008
March 27, 2008

Meeting Notes

Public Meeting – June 17, 2008

Interagency Task Force on Employee Misclassification

Unemployment Insurance Agency Problem Resolution Office – Lansing, Michigan

Task Force Attendees: Keith W. Cooley (Chair), Chris Peretto, Jack Finn, Craig Orr, Doug Schafer, Jack Nolish

The meeting was called to order at 2:00 p.m.

1. Approve Minutes from the March 27 & May 20, 2008 Meetings

There was one correction made on a Task Force member's name for the March 27th minutes. The minutes from March 27 and May 20, 2008 were approved by the committee.

2. Task Force Hearings

We made some plans for getting around the state with meetings starting the end of June into the fall. We want to coordinate with the Lt. Governor. The hearing dates are June 30th in the Detroit Metropolitan area, July 10th in Benton Harbor and September 16th in Lansing. We will also have meetings in Marquette, Traverse City and the Saginaw/Flint area. We have a location in mind for the Detroit Metropolitan area, but the availability has to be confirmed.

Q – Would the meetings be at 2:00 or at different times?

A – We want to stay around the same time for each meeting. We will try to keep them around 2:00.

3. Report out from

■ Legal Subcommittee

Jack Nolish/Jack Finn reported that the Legal Sub Committee met two times and discussed what the definition of an employee is. Wage and Hour and Worker's Comp have their own definitions of what a worker is. When the chair returns from leave, they will continue to work on the legislative interpretation of what an employee is. Director Cooley suggested we put that list of definitions for misclassification into a form that we can use and put into the report for the Governor.

■ Education Subcommittee

The Education Sub Committee met and teleconferenced with Norm Isotalo last Thursday to discuss the best way to educate the public. They want to educate the public, share information with other committees and share what the situation is currently and what the law is. They are trying to compile a list of major case laws. They want to work with other groups that may be interested in the area of Employee Misclassification. They may contact other groups and give them updates on the notes after the Governor has had a chance to review them. They may also use Power Point presentations if the Task Force agrees and use them at the beginning of the meetings. The board thought it was a good idea. Jack Finn will get a sample together. Director Cooley suggested that the Consumers' Corner also be a used to get information out.

- **Research Subcommittee**

Chris Peretto reported that the committee is getting the most recent information on employee misclassification, reviewing studies on what other states are doing to find out their best and worse practices, working with the IRS, reviewing methods of enforcement and researching the underground economy. They are tentatively expecting to have their next meeting the week of July 7th.

Director Cooley requested a concise complete report from all three committees on where we have been and where we are going by the July meeting and also asked that people volunteer for one of the committees. Director Cooley said we need another subcommittee on Enforcement. We will need guidelines to share with our state boards on how we are going to move forward.

4. MIOSHA's Link to Misclassification

Bob Pawlowski reported that MIOSHA's definition of an employer is an entity that allows one or more persons to work. An employee is defined as someone who is allowed to work. There is a legal precedence. They are looking at the company who employs the individual to do the work. They look at who's directing the work and who is providing remuneration for the people doing the work.

Q – Is there a legal test that you do to determine who the responsible party is?

A – We look at who's directing the work, who's providing direction, and who is providing payment and a number of other things.

Q – Do you know if your statute has anything that would limit you once you identify one of these cases from notifying another state agency?

A – We can do that. Right now we are doing that with Workers Comp.

Q – Can you make referrals to other agencies?

A – Yes. We have a process in place where we have an optional information code.

Q – Would you be looking at whether they are following MIOSHA safety standards, and other things like whether or not they have workers comp?

A – If during an investigation something comes out, we would notify that agency. We don't actively seek out other site issues.

Q – Is this limited to companies that have a certain number of employees?

A – No, we look at all employers. There are some provisions where we cannot look at employers with less than 10 employees, and certain north American classification codes, but that has to do with federal funding.

Q – Do you get complaints from workers on the site?

A – Yes, and when we do we make referrals to other agencies.

Q – Knowing what you know, what is your take on misclassification?

A – From MIOSHA's perspective, it is a problem on occasion. Bob Pawlowski said he would be interested in joining the Enforcement Subcommittee.

5. Discuss Ramifications of Misclassification and Tools for Enforcement

- Chris Peretto, UIA reported they have several different entities that are affected. If somebody is unemployed and they have a 1099 they are not covered they are not eligible for unemployment insurance. From the employer's perspective, if they pay someone on a 1099 and not as an employee, they are saving all sorts of taxes. Employers are probably not paying workers comp, not paying into the Trust Fund. Other employers are affected because they are paying a larger

amount because other businesses are not paying. What we do is if a person files a claim as a 1099 and there are no wages, we would have someone from the Field Audit unit go to that business and make a liability determination. It affects everyone in that situation. We do random audits and targeted audits where we get information from the IRS and tips from all over including from other employers.

Q- What are the penalties on something like that?

A- We have a statute that lets us go up to 4 times the amount of what they should have paid as a penalty, but we have to prove fraud and that it was intentional.

Q- How are you identifying the companies you mentioned you're investigating?

A - We get a lot of our information from the IRS. We are finding people who have been working as an employee are now being compensated under contract.

Q - Bart Carrigan, Associated General Contractors, asked if the company arranged for the employee to lease or own a vehicle, is that person considered an independent contractor?

A - We have eight different items that we look at to try to determine if someone is an employee or an independent contractor.

- Jack Nolish, Director, Workers' Compensation, stated the definition of an employee is very broad. If a worker does not maintain a separate business, does not hold himself out to render service to the public and does not employ other workers, he will be considered an employee. There are employers who say they are not employers but have a sub contractor and therefore don't need workers' comp or unemployment insurance. The information comes to us in a variety of ways and goes to the Compliance Division. Employers can be fined \$1,000 per day or punished by six months in jail through the AGs office and they can shut down their business. The other misclassification that goes on is between the insurance companies and employers. Underreporting of the number of employees goes on. It is a question of coverage or not. Employers can be fined, sanctioned or shut down. Workers' Compensation can go after someone personally. If you have suspicions about an employer's insurance coverage, you can go to the website www.michigan.gov/wca under insurance lookup.
- The Youth Employment Standard Act is easily defined. The Prevailing Wage Rate is where you find the greatest employee misclassification. The employer may sub contract out and the sub contractor may say everyone is an independent contractor but unfortunately there is very little enforcement. We don't have any penalties or enforcement actions at this time. The Payment of Wages and Fringe Benefit Act – if they find out, there are penalties and interest on that. The Minimum Wage and Overtime Law – There are penalties and provisions in that act we can enforce.

Q – On the prevailing wage for electricians, we were told by Wage and Hour that they don't get into classifications. Can the new task force take care of things like that now?

A – Wage and Hour doesn't have the authority to get into what type of work a job should be labeled as. There are jurisdictional issues.

Director Cooley said that issue may need to go to the Governor.

- Craig Orr from DMB reported that Business Services provides services for the state including purchasing goods and services, managing vehicle fleet, print and graphics and mail and deliver services. They are impacted by misclassification in the area of contracts for products and services. Prevailing wages come into play when employees may not be represented appropriately in the labor market and not getting the appropriate prevailing wages. Our primary enforcement tool that we have in place is that the contracts require vendors provide documentation that they have the necessary insurance coverage. If they don't, the contract is not implemented.

Q – Is there a requirement for a certified payroll?

A – It's required if DMB makes the request. It is not something that is routinely requested.

Q – Does the subcontractor have to register?

A – Yes

Q – What happens if the contract on the prevailing wage claims one or two employees and classifies eight or nine other people as sub contractors and don't include the others on the audit?

A – If something like that is reported, it could be grounds for termination of the contract.

Comment – In the Electrical Division, Public Act 217 requires you to hold a contractor's license, to be considered a contractor. That might help the Task Force.

Doug Schafer, Department of Treasury – If employers are paying employees under the table, the potential tax implications include non-payment of Withholding Tax and Single Business Tax. If employers are paying employees under the table, it is likely the compensation is paid from unreported cash receipts, which could also mean the employer is also underpaying sales tax if a retail business, and their own individual income taxes.

If an individual is misclassified as an independent contractor, that person may be claiming various expenses for meals, mileage etc., on a Schedule C, that they are not entitled to claim, which results in underpayment of income tax. If the individual is being paid cash, it is likely they are not reporting the cash wages on their individual income tax return.

The Tax Compliance Bureau enforces compliance to Michigan's Tax Statutes through its Large and Mid-size Business Division, Small Business and Special Teams Division, and the Discovery and Tax Enforcement Division.

We have a staff of 307 including 230 auditors that do compliance audits and projects. The Discovery and Tax Enforcement Division uses both legacy data and third party information to identify taxpayers that are non-filers or tax under reporters. The penalties imposed for non-compliance vary from 10% of the tax liability to 100%.

Q – New Michigan Business Tax – What, if any, is the difference for employees? Are there any incentives to misclassify employees?

A – There are no incentives because compensation is not part of the tax base.

Q – With all the penalties for employers, is there a reward program?

A – No.

Q – Do you find a lot of companies are going bankrupt to avoid tax obligations?

A – The Revenue Act has provisions for both officer liability and successor liability that

limits the opportunities to avoid payment of taxes through bankruptcy.

Q – How are businesses selected?

A – We have a sophisticated selection system that analyzes all businesses for audit assignment every account is judged fairly. By statute, we cannot disclose the selection criteria.

6. Approval of Report Outline

Director Cooley said we are on track to have the report to the Governor. There is an outline on the back table. We won't be saying much more on it until we get the report done.

7. Misclassification in the News

Norman Isotalo passed out a summary of articles regarding employee misclassification. Some of the articles dealt with legislation that has been introduced nationally and is intended to address the issue of properly classifying employees. Many of the articles contained information from other states. One article stated the teamsters endorse the program. Senator Obama has introduced legislation that is looking at the issue of misclassification.

8. Public Suggestions/Ideas/Comments

Q – If the employee reports a 1099 is there a greater penalty on the employee or employer, or are they penalized equally?

A – If the employee declares wages and paid tax, there would not be a liability as long as they pay the taxes. 1099 wages do not qualify for unemployment, but it could raise an issue for the employer if they didn't report the wages.

Comment: Sometimes people don't understand they are supposed to report the taxes as an independent contractor. When someone finds out, enforcement is just as strong against the employee as the employer. There should be some way to look at the employee in a different light so they will come forward. There needs to be some type of whistle blower type protection for employees.

Q – Todd McCastle, Carpenters, is there a contact number for Discovery Tax Division for Treasury?

A – The number is (517) 636-4120. There is also a fraud line.

Q – Do you have a way to file a complaint yet through the Task Force?

A – Enforcement is taking place as we speak. You can always file a complaint. UIA has a fraud hotline on their web page that is also set up for the Task Force. The hotline number is (800) 822-1122. If you call that number, the information will be shared with the Task Force.

Q – When is it proper to use a 1099?

A – If you have a legitimate independent contract worker, i.e. sales people, real estate agents, insurance salesmen etc., it would make sense to use a 1099 because they represent multiple businesses. The state follows IRS guidelines.

Q – Does the IRS get SS8s?

A – We might get them because of our exchange of information.

Q – If a subcontractor pays an individual who then pays a crew, the main boss may get a tax bill for \$10,000 that really wasn't his wages. What happens then?

A – With an undocumented work force, we would have to follow the paper trail.

9. Next Meeting Date and Location

It was suggested that the next meeting be in September in conjunction with the Lansing Public Hearing.

Q – Will the July report be disseminated?

A – It will be posted on the web site. If you leave us your e-mail address, we will send you copy of the report.

The meeting was adjourned at 3:35 p.m.

Meeting Notes

Public Meeting -- May 20, 2008

Interagency Task Force on Employee Misclassification

Lansing Unemployment Insurance Agency Problem Resolution Office

Director Cooley called the meeting to order at 2:00 p.m.

Committee members present: Keith Cooley, Chris Peretto, Bruno Czurka, Jack Flynn

#1 Meeting minutes were not available from the March 27, 2008 meeting for approval. They will be forwarded.

#2 Task Force Hearings

Hearing should be held in several places throughout the State Of Michigan.

Suggestions are: SE Michigan/Detroit area, Lansing, Grand Rapids/Kalamazoo, Saginaw/Bay City, Marquette, Petoskey/Traverse City, Sault St. Marie

These meetings should be held in a two to three month time frame preferably June through September. Things that need to be considered are: What is the best use of the time? How long should the meetings last?

#3 Set Date for Next Task Force Meeting

The next meeting for the task force will need a quorum of voting members. The first week in June is suggested, Deputy Director Corbin will coordinate the dates with members, tentatively will be the first week of June.

#4 Report out from Legal Subcommittee

Handouts were given listing the various legal definitions of an employee and the tests used to determine this.

Discussion

What way do these three different definitions overlap and how does it aid or hinder looking at companies to see if they have acted contrary.

Question from audience:

Will these be broken down into trades and professions such as mortgage brokers? In some cases they are given both 1099's and a W-2 for the same year.

Answer Director Cooley:

We would like to find a general definition that is useful to most and then apply it to special cases, we will look into it.

Discussion:

We may need more statutory authority to proceed with our plan. Is there any overlaps on the various rules that are already in place?

#5 Employee Misclassification in the News

Handouts of News clips from around the country regarding employee misclassification. Points of interest are 25% of New York City employees are off the books and what the related loss of tax and other revenue is as a result.

#6 Review of QETP Meeting

The meeting was held on May 6, 7, 8 in Washington DC. Attending were representatives from California, New York, Michigan and IRS, FTA and DOL representatives. This meeting is held two times a year. Next meeting is in November. The Feds are working hand-in-hand with States regarding misclassification of employees. Thirty-Two states have signed a Memorandum Of Understanding (MOU) to participate at this time and more are interested.

Question

How much is recovered as a result of the task force per year in these states?

Answer

We don't know but will try and get the information for the next meeting.

Question

Can others participate in the next informational call for this committee?

Answer

We will let the involved agencies know when the next call is so that they may participate.

Question

Could posters be placed in work sites to employees know about misclassification?

Answer

We will check, most posting are statutory in nature.

#7 Report on Web Site Activity – There have been 603 hits in the last 30 days with minimum exposure and 2 calls to the hotline. Work is being done on the site to develop a fill in the blank form so that necessary information is received at first contact and it will also allow anonymous reports.

Comment

Attorney General Cox has a place in his site for such reports, we could check to see if we can use that site or develop ideas from them. Maybe a link between the two.

#8 Report on Sharing Information and Referrals between Task Force Agencies

An advantage of sharing information is that it helps Workers Compensation make determinations with limited staffing; this helps us all with enforcement.

#9 Activities in Other States

Michigan has been contacted by Ohio wanting to know how we are setting things up and we are helping them get started.

Comment

Joyce has gotten contacts from New York and Texas to collaborate. Michigan has also met with the IRS to find better ways to share information with each other.

IRS will be invited to the next meeting to share information with us and Michigan is also sharing this information with other states. We have to be careful of information shared with other states due to revenue sharing concerns.

Comment

Director Cooley requested a time line for freely sharing information with Feds and other states.

Comment:

Chris Peretto reports that the Taskforce is really ramping up, they have close 478 cases already this year.

#10 Form -- Education and Research Sub Committees

Two additional subcommittees are needed for -Education and Research. Jack Finn indicated he would chair the Form Education and Chris Peretto indicated UIA would take the Research. A sign up sheet for the audience to volunteer for the committees was put on the table in the back of the room for others to sign up.

Comment

Director Colley suggested we e-mail those attending the last meeting so they would have an opportunity to sign up also. The subcommittees should meet before the next Taskforce meeting.

#11 Public Suggestions/Ideas/Comments

Comment

Eric Lanterman, a truck driver, relayed his experience recently with his employer regarding misclassification. He and his coworkers were told they had to sign an agreement to become independent contractors. He and 8 others refused and were fired as a result.

Question

How closely is the SUTA Unit working with the Taskforce?

Answer

SUTA and the Taskforce is the same Unit. They investigate each thing when ever they get a complaint.

Comment

The Michigan Carpenters Union suggested that they had a lot of information on companies that were misclassifying employees and they are willing to share that information with the Taskforce. This offer was accepted by the Taskforce and it was requested they send the top five employers information to start with.

Meeting was adjourned at 3:45 p.m.

Meeting Notes

Public Meeting -- March 27, 2008

Interagency Task Force on Employee Misclassification

Cadillac Place – Detroit, Michigan

Task Force Attendees: Keith W. Cooley (Chair), Jack Finn, Doug Schafer, Liza Estlund Olson, Craig Orr, Jack Nolish

Attendees: Gregg Whittet, Douglas Schafer, Jill McDougall, Department of Treasury; Chris Peretto, Tina Alagna, Neil Zechman, Joyce Surprenant, Mark Carlin, Linda Kalinowski, Rodger Palm, Linda Karos, UIA; Jack Minor, AFL-CIO; Mike Jackson, Michigan Carpenters; William Black, Teamsters; Dan Argentati, Michigan Fair Contracting Center, Jim Walker, GLFEA

Opening Statements from Director Cooley

This is an interagency Task Force on employee misclassification as you well know, and it was put together as a response to an Executive Order from Governor Granholm, Executive Order 2008-1 issued last month. We pulled together a number of subject matter experts to work on the issue of misclassification, look for ways to improve communication, make the public aware of the problem by coordinating and strengthening enforcement mechanisms and making recommendations for legislative changes wherever they may be needed. We have a requirement to have a report out this summer around July 1st, and annually thereafter.

Today's meeting is organizational. We are looking at a Task Force website (www.michigan.gov/dleg). There is a link to "Spotlight" that will take you to the materials on misclassification of wages. We've developed a Fact Sheet on how to tell if a particular circumstance involves misclassification of wages. We've established a fraud hotline to collect tips on potential employee misclassification, and we've started work on an e-mail hotline to collect additional tips.

I. Introductions

The committee introduced themselves, Jack Finn, Administrator, Wage & Hour; Doug Schafer, Director Tax Compliance Bureau with Michigan Dept of Treasury; Liza Estlund Olson, Acting Director of UIA; Keith Cooley, DLEG; Craig Orr, DMB Director of Business Service; Jack Nolish, Director, Workers' Compensation. Sharon Bommarito, Susan Corbin, and Chris Peretto were also introduced.

II. Task Force Structure

Two things, first, it is important for the citizens of the state that we get these kinds of issues resolved, so we're not prepared to make this a permanent convening body. We would like very much to find a way in the next two or three years, through either very good education or very strong enforcement to make this issue go away.

Secondly, this work is aimed at what we believe to be a small group of employers in Michigan. Most Michigan employers are trying to do the right thing to make themselves a success, make their company a success, make the state a success and to help to give the folks that work for them reasonable wages for reasonable work. So we don't want anyone to think that we believe that this is a majority.

■ Task Force Staffing

In addition to the staff at the table, Joyce Surprenant will be the lead staff person to help us in our work. She's a new manager in the SUTA unit, and will be working with the UIA's misclassification unit. Norm Isotalo is our Public Information Officer in Sharon's area. He will be responsible for communications, helping us to drive the education effort, and helping us to draft our final reports that have to go to the Governor.

■ Committees

It is our intent to put together several committees together to help us through our work.

- ▶ An Education/Communications committee to handle public education, and a web site.
- ▶ A Research Committee to see what's been done in Michigan and in other states.
- ▶ A Legal committee – an internal committee from the Task Force agencies that would review various laws, suggest possible changes to state laws & administrative rulings, and examine the issue of sharing confidential information.
- ▶ Advisory Groups – while they would not necessarily be official members of this Task Force, we think advice and council from those of you who find this issue worrisome would be important for us.

If there are other committees you think would make sense, please feel free to let us know. We have a sign up sheet for Education and Research, which are the main two that need public participation.

III. Schedule

■ Task Force Meetings

We are three short months away. I recommend that we have monthly meetings of the Task Force at least until we get the first report done and then look at meeting every other month after that on a yearly basis.

■ Committee Meetings

The committee meetings will have to happen at a faster pace and a faster cadence. We will have committees meet before the next Task Force meeting to be able to report back to the Task Force. My guess is it may be bi-weekly in order for us to have a good strong draft for the Governor in the first or second week of June time frame.

■ Public Hearings

We think it is appropriate to have public hearings. We hope to have advance notices go out days before the normal 18 to 24 hour advance notice. We suggest that the first one be held some time the week of May 19th. We have to try to decide what locations make the most sense considering the work that we have to do. There will be occasions when we will want to go throughout the state. We want to be in the areas where a hot bed of activity around misclassification is apparent so we can hear from the people who are most affected. Start thinking about if the week of May 19th makes sense and let us know.

Question: Will there be a mechanism through which the public will be able to communicate with this Task Force or the committees? Will there be the ability for the public to email or give you feedback through maybe your website?

Answer: There will have to be. Norm Isotalo is the contact for anyone who wants to bring information to the Task Force. We will make arrangements for e-mail as well as for snail mail input.

IV. Next Steps

There will have to be at least two time lines, one that gets us from here to July 1st and then another one that drives us in a regular cadence over the years to come. We need input from our customer base in terms of where in the time line certain

events or certain issues ought to be driven to the top of the pile. We will be looking for any suggestions/advice you have. We will be putting together an inventory of resources that will be at our disposal, such as laws, regulations and statutes that would be available for us to use in this work. We hope to have that ready for the next meeting. We will be scheduling and organizing the public hearings and arranging for the first one to take place, and scheduling the committee meetings.

V. Public Comment

The following public comments were made:

(William Black)

"My name is William Black, Executive Director of Michigan Teamsters Joint council No. 43 D.R.I.V.E. First and foremost thank Governor Jennifer Granholm for her leadership in signing Executive Order 2008-1 creating the Interagency Task Force on Employee Misclassification and also, we want to thank Director Keith W. Cooley for his leadership and work that he's putting in this Task Force along with all the Task Force members. We want to thank you for your efforts and we look forward to working hand in hand with you in this. I appear before you today to request your assistance in regards to an endemic problem of misclassification of employees as independent contractors, a deep and sad growing problem which seriously impacts the economy of our state and our nation as a whole.

On behalf of the International Brotherhood of Teamsters and General President James P. Hoffa, which represents 1.4 million working men and women in this country and 90,000 active and retired members in Michigan, I can tell you that the teamsters are painfully aware of the widespread misclassification of workers in this state to avoid the costs of state and federal labor and tax laws.

In our industries, some of them which are very familiar to this Task Force such companies as Brownberry in the Bakery industry and FedEx Ground in the freight industry openly operate in Michigan as misclassified workers are completely exempt from unionization, simply because they are "mislabeling" by the companies. Indeed, nonunion drivers of Brownberry on both the east side and west side of Detroit pull out of our union facilities and deliver bakery products every single day just as our union drivers do. But simply because the company calls them "independent distributors," they have no right to join a union, they have no protection from the labor laws as employees do, and there is no end in sight for them of relief of this situation.

Moreover, around the country companies in the baking industry such as Sara Lee, somebody that we've all heard and probably ate their products, have "converted" workers from employees to independent contractors for that very purpose. Even workers under union contracts today have been reclassified to skirt labor laws and other laws that would protect them.

As you may very well have read in press accounts, very large employers such as Federal Express have been caught red handed misclassifying workers on a wholesale basis. Recently, the Internal Revenue Service fined the company

\$315 million dollars for such wrongful misclassification of its drivers. Because of such behavior all around the country, misclassified workers lose out on the protection of minimum wage and overtime laws, workers' compensation and unemployment insurance, health and safety laws, discrimination laws, and the right to bargain collectively to form a union.

Correspondingly, states such as Michigan lose out on payroll and related taxes at a time when our state desperately needs money. They also lose out on premiums for workers compensation and unemployment. Moreover, and I want to make sure that this point is delivered very clearly, law abiding employers who play by the rules lose out because of unfair competitive advantages gained by companies who misclassify their workers to skirt labor and tax regulation.

That is why I'm urging you, on behalf of our union and the working men and women of this state, to vigorously investigate the employers in our state who engage in such illegal activity. Most recently, in December 2007 the Massachusetts Attorney General Martha Coakley's office assessed penalties of more than \$190,000 against FedEx Ground for intentionally misclassifying thirteen drivers as independent contractors. In our opinion, such action represents a beneficial, proactive approach to this serious problem by Attorney General Coakley who stated, "The practice of misclassification does great harm, not only to the misclassified workers and to the Commonwealth in the form of lost revenues, but here again, but also by putting law-abiding businesses at a disadvantage. We intend to pursue aggressively employers such as FedEx Ground when they violate the Commonwealth's Independent Contractor Law." The Attorney General's office in New York has taken very similar steps to addressing this problem. But we all need to work together on this issue to solve it, and to make the good employers more competitive.

We believe that through increased enforcement through our laws as we suggested, along with an active and concerted effort envisioned by our great Governor, that together we can turn the tide of misclassification in Michigan and this country, which is an economic and moral imperative. We believe that with combined and coordinated efforts by the myriad of state agencies which are charged with the duty of administering our labor laws, Michigan will not only reap the reward of recaptured revenue that has wrongfully been withheld from state coffers because of illegal activity, but also employers will be deterred from taking such illegal actions in the future. Accordingly, we urge you to take immediate action on behalf of the fine and hard-working citizens of Michigan.

For this we look forward to working with this committee. We will make ourselves available at any time and any place to support this, whether it's on the 19th or whenever we will be available. We look forward to working with you and that concludes my comments."

(Jack Minor)

"I'll be very informal. I didn't prepare testimony, but Jack Minor, Legislative Director of Michigan AFLCIO, I certainly concur with the comments made by Mr. Black. We found that the problem occurs also in Building Trades frequently where people are listed as independent contractors including operating large vehicle or large equipment who clearly don't bring their Caterpillar or their crane

to work in the morning as their own tools, which is one of the definitions. I want to stress that in particular this is a – I want to stress the unfairness to those businesses who operate legitimately. It's the employer who actually uses the Independent Contractor escapes enormous costs whether it's workers comp, or social security taxes or health coverage and so on. And I also want to stress that in my experience, I found as a former legislator, that there was a proposal which the legitimate temp employees, the Kelly services if you will fought very hard but it was really an attempt to legitimize having any employee classified as a temp employee and I think that is a concern that we also want to watch weather it's in offices non unionized certainly but a number of areas. And finally, I want to ask if there will be an opportunity for Whistle Blowers if you will people who are and again I use the term "employed" with quotes, "employed" who understand that they are misclassified and who would like to register a complaint, but understand also that they have no protections because they're an "independent contractor" and that ought to be in quotes also. So I hope there will be an opportunity for Whistle Blower type testimony. Thank you."

(Response)

To Mr. Miner's point, the Whistle Blowers piece will probably be key to our being able to do a good job with this. We will certainly take testimony. Anyone who wants to make a phone call to us to help us understand the gravity or severity of problems wherever they may be, we will be very much interested in that. And we will do whatever we can inside of the existing laws to make sure that those kinds of Whistle Blowers don't suffer extreme treatment or severe treatment because they've spoken up on behalf of their friends and others who are just trying to make sure that the laws are obeyed. Thank you all very much for being here and we really look forward to working closely with you as we tackle this job we're on. Thank you.